MOODY'S
INVESTORS SERVICE

Rating Action: Moody's changes Ghana's outlook to positive from stable, affirms B3 rating

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New York, January 24, 2020 -- Moody's Investors Service ("Moody's") has today affirmed the Government of Ghana's long-term issuer and senior unsecured bond ratings at B3 and changed the outlook to positive from stable. Moody's has concurrently affirmed the rating of the bond enhanced by a partial guarantee from the International Development Association (IDA, Aaa stable) at B1.

The decision to assign a positive outlook reflects Moody's rising confidence that the country's institutions and policy settings will foster improved macroeconomic and fiscal stability over the medium term, in part as a consequence of the reforms implemented under the recent IMF reform program. Those reforms are beginning to bear fruit, as seen for example in the return to primary fiscal surpluses, measures to smooth the debt maturity profile and increasingly sustainable growth prospects. Pressures and risks remain, as evidenced by persistent revenue challenges, a potential repeat of pre-election fiscal cycles, and the emergence of significant arrears and further contingent liabilities in the energy sector, all contributing to rising public debt. The positive outlook reflects increasing confidence that the government will manage those pressures in such a way as to sustain and enhance external and fiscal stability.

The decision to affirm the B3 rating balances, for now, those positive medium-term trends and existing challenges. A key constraint on the rating is the country's significant exposure to international capital flow reversals, which tend to coincide with exchange rate volatility and rising external and domestic borrowing costs, putting pressure on already weak debt affordability. Measures which reduce that exposure by demonstrating reliable liquidity risk management and increasingly firm control over the debt position would support an upgrade to a B2 rating. However, those measures will take time to evidence impact. As a consequence, the outlook is unlikely to be resolved quickly and may even extend beyond the usual 18 month period in order to monitor how policy unfolds following the forthcoming election, and in particular the government's progress in implementing its energy recovery strategy.

Ghana's foreign- and local-currency bond and deposit ceilings remain unchanged, namely the foreign-currency bond ceiling at B1, the foreign-currency deposit ceiling at Caa1, and the local-currency bond and deposit ceilings at Ba3.

RATINGS RATIONALE

RATIONALE FOR THE POSITIVE OUTLOOK

RISING CONFIDENCE THAT POLICYMAKERS WILL SUSTAIN ECONOMIC AND FINANCIAL STABILITY

For some time, Ghana's rating has been constrained by two related factors. First, by the challenges its policymaking institutions have experienced in establishing a consistent set of policies which support macroeconomic and financial stability, and which survive changes of government. Second, by the high level of external commercial debt holdings which, taken alongside limited net foreign exchange reserves, exposes the government and the balance of payments to a loss of international investors' confidence in policymakers' ability to sustain economic and financial stability, raising the risk of a fiscal and/or balance of payments crisis.

However, in recent years Ghana has seen a number of positive developments in key credit metrics, which partly reflect the institutional and fiscal reforms implemented under the four-year IMF program that was completed in April 2019. These include a return to sustained economic growth at around 5% on average, supported by the development of domestic hydrocarbon resources and the prospect of sustained non-oil growth driven by the restoration of power supply and renewed infrastructure investment, a structural improvement in the current account dynamics, and fiscal reforms which have resulted in primary surpluses since 2017.

Key fiscal reforms include the Public Financial Management Act (2016) which improves fiscal governance and the Fiscal Responsibility Law (2018) requiring adherence to an overall fiscal deficit ceiling of 5% of GDP and a primary surplus. 2019 saw a cash deficit of 4.8% of GDP and a primary surplus of 0.9% of GDP -- weaker than the initial targets but within overall limits. Moody's expects a similar outcome this year and a renewed shift to fiscal consolidation following the election.

Beyond the fiscal sphere, measures taken over the past couple of years to recapitalize the financial sector and to address the country's power deficit (albeit the latter with problematic unintended consequences) also suggest active, moderately effective policymaking and support rising confidence in policymakers' ability to sustain economic and financial stability, and to limit the risk of external shocks in the coming years.

RATIONALE FOR AFFIRMING THE B3 RATING

Nevertheless, challenges remain, alongside developments which suggest that the roots of the institutional reforms are, for now at least, shallow. The rise in deficits in 2019 as the election approaches, as in past cycles, suggests a high likelihood that the usual pre-election fiscal stimulus will emerge in 2020. Fiscal targets have been achieved in part by recording as 'below the line' items fiscal costs relating to the recapitalization of the banking sector and to energy legacy debts which have caused the overall debt burden to continue to rise. The government is contemplating issuing additional, 'collateralised', debt to support investment in bauxite refining in part to absorb surplus energy.

As a result, the debt burden has risen by nearly ten percentage points of GDP since 2017, in part as a consequence of the financial sector bailout in 2018-19 and the measures taken to clear legacy power utility debts (estimated at 4.5% and 2% of GDP, respectively). Estimated at around 64% of GDP at end-2019, it is expected to rise further over the near term. How far and for how long it rises will depend in part on the government's success in preserving exchange rate stability and in dealing with additional contingent liabilities arising in the energy sector.

Those contingent liabilities arose from the agreement of 'take or pay' contracts with energy producers extending until 2023, which were entered as part of the measures taken to address the acute power shortages experienced earlier in the decade. While the power shortages were indeed alleviated and the consequent shadow over economic activity lifted, this was achieved under a program that incorporated overoptimistic estimates of power demand which have left the government bearing ongoing 'take or pay' costs. According to the government's Energy Sector Recovery Program (ESRP), under a business as usual scenario, the government faces annual costs of between $1.6 billion (2.3% of GDP) and $2.6 billion (3% of GDP) from 2020-23 which, added to outstanding energy sector arrears of $2.7 billion (or 4.1% of GDP) at the end of 2018 could sum to around $12.5 billion, or about 14% of GDP by 2023.

The government is contemplating a number of measures under the Energy Sector Recovery Program (ESRP) to reduce the fiscal impact of the annual financial shortfall in the energy sector without further increasing arrears. The likelihood of their being successful is unclear and some measures, including the finalization of the domestic energy infrastructure or the development of the Integrated Aluminium Strategy to boost demand, will likely require upfront investments that increase the debt load still further.

Moody's debt projections include an annual assumption of 2% of GDP in the form of contingent liabilities, implying a further increase in the debt ratio to over 65% of GDP by 2023. Moody's forecasts also include disbursements under the $2 billion financing deal with Sinohydro -- an infrastructure financing deal that is collateralized by the country's yet to be mined and refined bauxite resources -- at an assumed annual execution rate of about $100-$200 million in the funding requirements and in the debt ratio.

Overall, fiscal flexibility remains low. Since around 40% of the debt stock is denominated in foreign currency, the debt trajectory is sensitive to exchange rate shocks. At 15%, revenue-to-GDP remains low notwithstanding efforts -- and future plans -- to enhance tax collection. The government's borrowing requirement is moderate at around 16% of GDP annually, but it remains reliant on continued international capital market access to meet its funding needs in the future. Some of these challenges are mitigated by the government's maturity lengthening strategy and by the continued smoothing of the debt refinancing undertaken both in the domestic and external debt segments ahead of the next eurobond maturity due in 2023.

ENVIRONMENTAL SOCIAL AND GOVERNANCE CONSIDERATIONS

Environmental considerations are material for Ghana. The cocoa sector is a large contributor to GDP and to exports and remains an important source of employment. The weight of the agricultural sector exposes the economy to weather-related disruptions and (over the longer term) the effects of climate change.

Social considerations are not material for Ghana's credit profile. The country's improved development indicators over time have supported a relatively peaceful and democratic political backdrop, as reflected in our low assessment of political risk.

Governance considerations are material for Ghana's credit profile. As previously noted, the B3 rating partly reflects institutional challenges within the policymaking apparatus; conversely, the positive outlook reflects rising confidence that institutional reforms may be taking root.

FACTORS THAT COULD LEAD TO AN UPGRADE

Over the coming 1-2 years, Moody's will assess the government's willingness and capacity to arrest the rise in the debt burden and to sustain and deepen economic resilience. That assessment will take into account how far the government adheres to the letter and spirit of the Public Financial Management Act (PFMA) and Financial Responsibility Law (FRL), at least once the election is past, including through the transparent recording of off-budget and below-the-line transactions that create funding needs. It will, relatedly, take into account the government's success in mitigating the fiscal impact of energy sector contingent liabilities and arrears, and in improving revenue collection efforts.

Taken together, a set of measures that arrest the rise in the direct and contingent debt burden and give confidence that the burden will fall over time would support an upgrade to B2. Economic developments which enhance potential growth would also be credit supportive, as would indications from debt issuance that the government's efforts are garnering confidence among international investors on a sustained basis.

FACTORS THAT COULD LEAD TO A DOWNGRADE

Conversely, Moody's would likely return the outlook to stable at the B3 level should it conclude that the coming years will not see a more consistent, effective policymaking environment emerge. The disregard or undermining of fiscal rules, and the inability to achieve structural revenue-based improvements in the fiscal position or to mitigate downside risks arising from arrears and contingent liabilities would be important signals in this respect. Indications, such as falling demand or rising issuance costs, that external investors, on whom the government relies to service and refinance external debt, are losing confidence in the government's ability to sustain fiscal or economic resilience would similarly undermine the government's creditworthiness.

GDP per capita (PPP basis, US$): 6,492 (2018 Actual) (also known as Per Capita Income)

Real GDP growth (% change): 6.3% (2018 Actual) (also known as GDP Growth)

Inflation Rate (CPI, % change Dec/Dec): 9.4% (2018 Actual)

Gen. Gov. Financial Balance/GDP: -3.8% (2018 Actual) (also known as Fiscal Balance)

Current Account Balance/GDP: -3.1% (2018 Actual) (also known as External Balance)

External debt/GDP: 35.6% (2018 Actual)

Economic resiliency: ba3

Default history: No default events (on bonds or loans) have been recorded since 1983.

On 22 January 2020, a rating committee was called to discuss the rating of the Ghana, Government of. The main points raised during the discussion were: The issuer's economic fundamentals, including its economic strength, have increased. The issuer's institutions and governance strength, have not materially changed. The issuer's governance and/or management, have not materially changed. The issuer's fiscal or financial strength, including its debt profile, has not materially changed. The systemic risk in which the issuer operates has not materially changed. The issuer's susceptibility to event risks has not materially changed.

The principal methodology used in these ratings was Sovereign Ratings Methodology published in November 2019. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

The weighting of all rating factors is described in the methodology used in this credit rating action, if applicable.

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Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

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